Treasury Management Strategy Statement and Annual Investment Strategy Update 2020/21

The Treasury Management Strategy Statement (TMSS) for 2020/21 was approved by Council on 26th February 2020.

There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:
- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

Prudential Indicator for Capital Expenditure

The following table shows the revised estimates and financing of capital expenditure and the changes since the capital programme was agreed at the Budget. It also highlights the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure.

Capital Expenditure	2020-21 Original Programme £'000	2020-21 Latest Approved £'000	Actual As At 30-09-20 £'000	2020-21 Forecast Outturn £'000
Housing Revenue Account (HRA)	9,529	12,077	2,037	9,498
General Fund	3,795	6,080	509	5,498
Commercial activities/non-financial investments *	2,934	4,306	1	3,224
Total spend	**16,258**	**22,463**	**2,547**	**18,220**
Financed by:				
Capital receipts	3,114	3,114	990	3,114
HRA Capital receipts – Land Sales	410	410	-	410
Capital grants and Contributions	1,241	2,474	567	2,474
Major Repairs Reserve	3,235	5,416	614	5,416
Direct Revenue Funding	4,197	6,137	133	3,465
1-4-1 receipts	482	482	31	482
Shared Ownership Sale Proceeds	409	409	212	409
Total financing	**13,088**	**18,442**	**2,547**	**15,770**
Borrowing need	**3,170**	**4,021**	**-**	**2,450**

*Commercial activities/non-financial investments relate to areas such as capital expenditure on investment properties, loans to third parties etc.

The General Fund capital expenditure programme has increased from an original budget of £6.729m to £10.386m. The key items that have resulted in this increase were due to the roll over from the previous year and are as follows:

- Capital Acquisitions for Growth and Commercialisations £500k
- Welland Homes £851k
- Food Enterprise Zone £1.061m
- Housing Infrastructure Funding £1m

The borrowing need shown in the above table is the Council's purchase of an additional equity stake in Welland Homes and the loans made to Welland Homes. This capital expenditure has not been financed and therefore creates a borrowing requirement. Rather than take out external borrowing, the Council is utilising its cash balances and internally borrowing to finance the capital expenditure.

Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary.

The following table shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period. This is termed the Operational Boundary.

	2020-21 Original Estimate For Year End £'000	2020-21 Latest Approved For Year End £'000	Position As At 30-09-20 £'000	2020-21 Forecast Outturn For Year End £'000
Prudential Indicator – CFR				
CFR – housing	68,441	68,441	68,427	68,427
CFR – non housing	4,677	5,528	1,441	1,688
Commercial activities/ non-financial investments	8,410	8,410	5,124	7,327
Total CFR	**81,528**	**82,379**	**74,992**	**77,442**
Net movement in CFR	**3,170**	**4,021**	**-**	**2,450**
Prudential Indicator – External Debt / Operational Boundary				
Borrowing	67,456	67,456	67,456	67,456
Other long term liabilities	0	0	0	0
Total debt 31 March	**67,456**	**67,456**	**67,456**	**67,456**
Approved Operational Boundary	**87,000**	**87,000**	**87,000**	**87,000**

The original estimate for the CFR for 2020/21 in the table above was set prior to the year-end accounts for 2019/20 being completed. The position as at 30 September 2020 and the revised estimate therefore takes account of these adjustments.

Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2020/21 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

	2020-21 Original Estimate For Year End £'000	**2020-21 Revised Estimate For Year End £'000**	**Position As At 30/09/20 £'000**	**2020-21 Forecast Outturn For Year End £'000**
Gross borrowing	67,456	67,456	67,456	67,456
Less investments	(19,679)	(20,037)	(50,171)	(24,280)
Net borrowing	**47,777**	**47,419**	**17,285**	**43,176**
CFR (year-end position)	**81,528**	**82,379**	**74,992**	**77,442**

The Executive Director Commercialisation (Section 151 Officer) reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

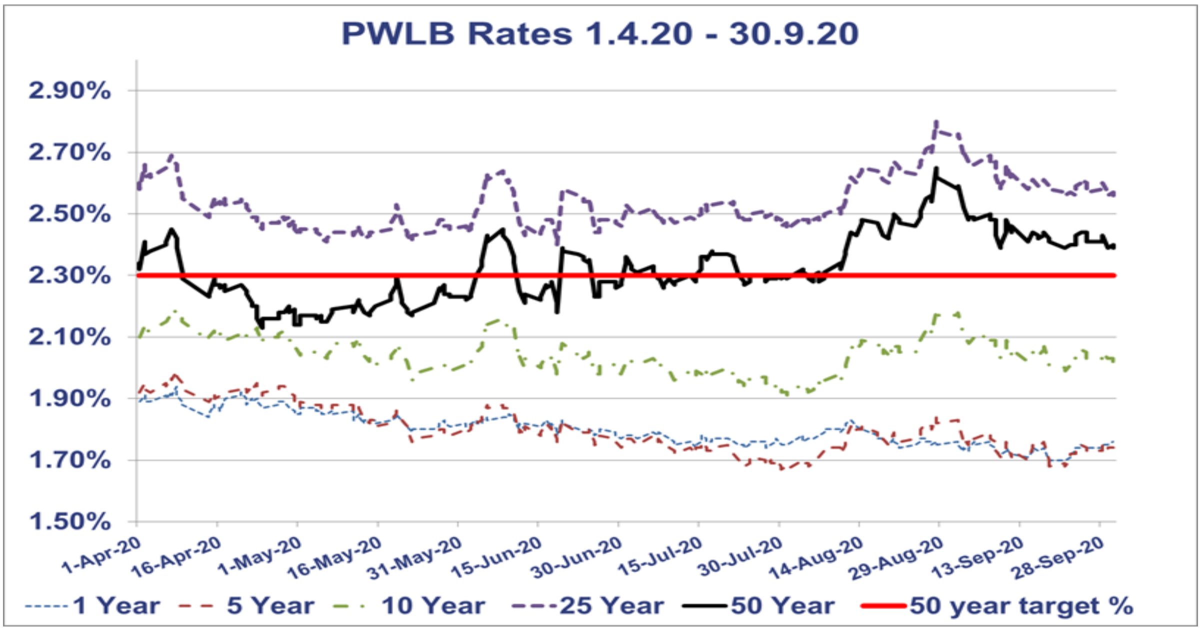
Authorised limit for external debt	**2020-21 Original Estimate For Year End £'000**	**Position As At 30/09/20 £'000**	**2020-21 Revised Estimate For Year End £'000**
Borrowing	85,000	85,000	85,000
Other long term liabilities	1,000	1,000	1,000
Commercial activities/non-financial investments	5,000	5,000	5,000
Total	**91,000**	**91,000**	**91,000**

The limit of £1m for long term liabilities shown above provides headroom for the Council to take out finance leases for capital assets rather than outright purchase. Prior to taking out a finance lease, a full option appraisal would be carried out to ensure it is the most cost effective way of financing the capital expenditure.

Borrowing

The Council's projected capital financing requirement (CFR) for the end of 2020/21 is £77.442m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board (PWLB) or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The Council has borrowings of £67.456m in respect of the Housing Revenue Account self-financing settlement and it is anticipated that further borrowing will not be undertaken during this financial year but this will be kept under review.

The following graph shows the movement in PWLB rates for the first six months of the year to 30th September 2020.



The 50-year PWLB target rate for new long-term borrowing was unchanged at 2.30%.

Debt Rescheduling

Debt rescheduling opportunities have been very limited in the current economic climate and following the various increases in the margins added to gilt yields which have impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

Compliance with Treasury and Prudential Limits

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30th September 2020, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2020. The Executive Director Commercialisation (Section 151 Officer) reports that no difficulties are envisaged for the current or future years in complying with these indicators.

<u>Annual Investment Strategy</u>

The Treasury Management Strategy Statement (TMSS) for 2020/21, which includes the Annual Investment Strategy, was approved by the Council on 26th February 2020. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap overlay information.

As shown by the interest rate forecasts in **Appendix B**, it is now impossible to earn the level of interest rates commonly seen in previous decades as all investment rates are barely above zero now that Bank Rate is at 0.10%, while some entities, including more recently the Debt Management Account Deposit Facility (DMADF), are offering negative rates of return in some shorter time periods. Given this risk environment and the fact that increases in Bank Rate are unlikely to occur before the end of the current forecast horizon of 31st March 2023, investment returns are expected to remain low.

Negative investment rates

While the Bank of England has said that it is unlikely to introduce a negative Bank Rate, at least in the next 6 -12 months, some deposit accounts are already offering negative rates for shorter periods. As part of the response to the pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the Covid crisis; this has caused some local authorities to have sudden large increases in investment balances searching for an investment home, some of which was only very short term until those sums were able to be passed on.

As for money market funds (MMFs), yields have continued to drift lower. Some managers have suggested that they might resort to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a glut of money swilling around at the very short end of the market. This has seen a number of market operators, now including the DMADF, offer nil or negative rates for very short term maturities. This is not universal, and MMFs are still offering a marginally positive return, as are a number of financial institutions.

Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

Investment Portfolio 2020/21

The Council held £50.171m of investments and £3.227m of loans to Welland Homes as at 30 September 2020. The investment portfolio yield for the first six months of the year is 0.756% against a benchmark of 0.106% (average 3 month LIBID). Deposits held excluding accrued interest are shown on the following page.

In addition to the investments listed, the Council has issued four loans to Welland Homes totalling £3.227m at a rate of 3.5% which are classified as Long Term Debtors.

The Executive Director Commercialisation (Section 151 Officer) confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2020/21.

The Council's budgeted investment return for 2020/21 is £544,200 (GF £383,000, HRA £161,200) and performance for the year to date is £202,340 which is £70,000 below the profiled budget. The outturn is currently projected to be £325,000 which is £219,200 below the estimate. This budget shortfall can be attributed to the current level of exceptionally low interest rates available.

The Council monitors risk of its investment portfolio against the Link Asset Services counterparty risk matrix. This matrix gives recommended maximum investment durations for each financial institution based on the ratings allocated by the major credit rating agencies and also takes into account credit default swap prices.

Institution	Investment Type	Start Date	Maturity Date	Rate/ Return %	As at 31-03-20 £'000	As at 30-09-20 £'000
Welland Homes (Fair Value)	Equity	n/a	n/a	n/a	2,601	2,601
South Holland Community Housing Company (Fair Value)	Equity	n/a	n/a	n/a	1,063	1,063
Lloyds Bank Current Account (A+)	Instant Access	n/a	n/a	0.00	514	1,023
Handelsbanken (AA)	Instant Access	n/a	n/a	0.10	4,999	4,992
CCLA Money Market Fund	Instant Access	n/a	n/a	0.12	6,190	10,000
Lloyds Bank (A+)	95 Day Notice	n/a	n/a	0.20	0	2,492
Lloyds Bank (A+)	Time Deposit	12/04/19	09/04/20	1.25	2,500	0
National Westminster Bank (A+)	Certificate of Deposit	19/06/19	17/06/20	1.00	5,000	0
Standard Chartered (A+)	Time Deposit	10/10/19	09/04/20	0.82	3,000	0
Lloyds Bank (A+)	Time Deposit	21/11/19	20/11/20	1.10	2,500	2,500
Helaba Bank (A+)	Time Deposit	02/12/19	02/12/20	0.89	2,500	2,500
Goldman Sachs International Bank (A)	Time Deposit	13/12/19	12/06/20	0.96	3,000	0
Australia & New Zealand Bank (A+)	Time Deposit	07/01/20	05/01/21	0.97	2,500	2,500
Nationwide Building Society (A)	Time Deposit	30/01/20	30/07/20	0.74	3,000	0
Thurrock Borough Council (N/A)	Time Deposit	13/03/20	12/03/21	1.05	2,000	2,000
Close Brothers (A-)	Time Deposit	08/04/20	08/10/20	1.25	0	2,500
Standard Chartered (A+)	Time Deposit	20/04/20	20/10/20	1.11	0	3,000
Doncaster Metropolitan Borough Council (N/A)	Time Deposit	13/05/20	12/05/21	1.00	0	3,000
Standard Chartered (A+)	Time Deposit	12/06/20	17/03/21	0.41	0	2,000
National Westminster Bank (A+)	Certificate of Deposit	17/06/20	17/03/21	0.39	0	5,000
Nationwide Building Society (A)	Time Deposit	29/09/20	07/01/21	0.05	0	3,000
TOTAL					**41,367**	**50,171**

OTHER

Changes in risk policy

The 2018 CIPFA Codes and guidance notes have placed enhanced importance on risk management. Where an authority changes its risk policy e.g. for moving surplus cash into or out of certain types of investment funds or other types of investment instruments, this change in risk policy should be brought to members' attention in treasury management update reports.

There has been no change in risk policy to report.